THE STATE OF SOUTH CAROLINA
In the Supreme Court

APPEAL FROM THE PUBLIC SERVICE COMMISSION OF SOUTH CAROLINA

Public Service Commission Docket Nos. 2018-319-E & 2018-318-E

Duke Energy Carolinas, LLC ········ Appellant-Respondent,

v.

The South Carolina Office of Regulatory Staff, Hasala Dharmawardena, CMC Recycling, Cypress Creek Renewables, LLC, SC Department of Consumer Affairs, Sierra Club, South Carolina Coastal Conservation League, South Carolina Energy Users Committee, South Carolina Solar Business Alliance, Inc., the South Carolina State Conference of the National Association for the Advancement of Colored People, Upstate Forever, Vote Solar, and Walmart, Inc. ········ Respondents,

of whom,

South Carolina Energy Users Committee is ········ Respondent-Appellant.

Duke Energy Progress, LLC ········ Appellant,

v.

The South Carolina Office of Regulatory Staff, Nucor Steel-South Carolina, Cypress Creek Renewables, LLC, SC Department of Consumer Affairs, Sierra Club, South Carolina Coastal Conservation League, South Carolina Energy Users Committee, South Carolina Solar Business Alliance, Incorporated, The South Carolina State Conference of the National Association for the Advancement of Colored People, Upstate Forever, Vote Solar, and Walmart, Inc., ··Respondents.

**APPELLANTS' BRIEF OF DUKE ENERGY CAROLINAS, LLC AND DUKE ENERGY PROGRESS, LLC**

Heather Shirley Smith (SC Bar No. 102103)
Deputy General Counsel
Duke Energy Carolinas, LLC
Duke Energy Progress, LLC
40 West Broad St., Suite 690
Greenville, SC 29601
heather.smith@duke-energy.com

Frank R. Ellerbe, III (SC Bar No. 1866)
Robert E. Stepp (SC Bar No. 5335)
Robinson Gray Stepp & Laffitte, LLC
P.O. Box 11449
Columbia, SC 29211
fellerbe@robinsongray.com
rstepp@robinsongray.com

Sarah P. Spruill (SC Bar No. 68337)
Haynsworth Sinkler Boyd, P.A.
ONE North Main Street, 2nd Floor
Greenville, SC 29601
sspruill@hsblawfirm.com

Thomas S. Mullikin (SC Bar No. 7939)
Mullikin Law Firm
1308 Broad Street
Camden, SC 29020
tommullikin@mullikinlaw.com

Attorneys for Duke Energy Carolinas, LLC and
Duke Energy Progress, LLC

# TABLE OF CONTENTS

## TABLE OF AUTHORITIES

### CASES



### CONSTITUTIONAL PROVISIONS

## STATUTES



## REGULATIONS

## Other Authorities

## STATEMENT OF ISSUES ON APPEAL

1. Did the Public Service Commission err in disallowing prudently incurred coal ash compliance costs based solely on the Commission's determination that Duke Energy Carolinas, LLC and Duke Energy Progress, LLC should not be able to recover any expenses the Commission deemed to be incurred pursuant to the North Carolina Coal Ash Management Act?

2. Did the Public Service Commission err in disallowing certain coal ash compliance costs based not on any determination that the costs were not reasonably and prudently incurred but rather on the erroneous and speculative testimony of one witness as to which costs were incurred as a result of the North Carolina Coal Ash Management Act?

3. Did the Public Service Commission err in disallowing coal ash litigation expenses without giving Duke Energy Carolinas, LLC and Duke Energy Progress, LLC an ample opportunity to explain and justify these expenditures?

4. Did the Public Service Commission err in disallowing a return on approved deferrals of prudently incurred extraordinary costs?

## STATEMENT OF THE CASE

These consolidated appeals stem from the rulings of the Public Service Commission of South Carolina (the "PSC" or the "Commission") in the 2018 rate cases filed by Duke Energy Carolinas, LLC ("DEC") and Duke Energy Progress, LLC ("DEP") (collectively, the "Duke Entities" or the "Companies"). Although the evidence in these cases differs somewhat and the underlying orders are not identical, the PSC's rulings and the Duke Entities' arguments on appeal are substantively the same.

### I. DEC

On November 8, 2018, DEC filed an Application (the "DEC Application") with the PSC requesting authority to adjust and increase its electric rates, charges, and tariffs effective June 1, 2019. (R. at 3979-4008). The DEC Application sought the recovery through customer rates of various costs incurred by DEC and deferrals of other extraordinary costs. This appeal stems from the Commission's handling of the following requests: (1) DEC's request to recover deferred coal ash compliance costs incurred between January 1, 2015 through September 30, 2018 and estimated costs to be incurred from October 2018 through December 2018 plus deferred depreciation and a return on the deferred balances totaling $242 million on a South Carolina retail basis (*Id.* at ¶¶ 7, 11, 15, 20-21; R. at 4148:12-14)[1]; (2) DEC's request to recover $575,000 in litigation costs relating to coal ash (*see* R. at 4624:8-23, 4650:2-53:16); and (3) DEC's request to recover a return on certain deferred costs at a rate equal to its weighted average cost of capital ("WACC") (R. at 3979-4008 (¶¶ 15, 18, 20-21, 43-47)).

[1] The total DEC system coal ash compliance spend for this period was much higher, $958 million. (R. at 4148:3-6).

DEC and the South Carolina Office of Regulatory Staff ("ORS") agreed on many issues.[2] For example, DEC agreed with ORS to a Basic Facilities Charge ("BFC") of $11.96 for residential non-time of use, $13.09 for residential time of use, and $11.70 for small general service customers (as opposed to the $28 requested by DEC in the Application). (R. at 3902, 3908-09). DEC was willing to make this change after listening to the customer response to the original proposal.

However, on other matters, the parties were not able to reach an agreement. In addition, ORS took new positions with respect to the handling of certain items and departed from past practice and procedure without providing advance notice to DEC. On the issue of deferrals, ORS took the unprecedented position that DEC would not be entitled to any return on many of its deferred costs. ORS admitted this was a new policy that was not disclosed to DEC at the time of its Application. (R. at 4941:11-17). ORS further admitted that it planned in the future to request a generic docket that would set guidelines relating to deferrals on a prospective basis. (R. at 4941:18-42:7). With respect to coal ash litigation costs, DEC responded to ORS's discovery requests as written and was surprised to arrive at the hearing to discover that ORS was taking the position that these costs should be excluded because DEC had failed to meet its burden of proof. (R. at 4951:25-59:12).[3]

---

[2] Pages 16-19 of the Order include a summary of the areas of agreement and dispute between DEC and ORS as of the hearing. (R. at 3902-05). In addition, the Order includes a list of nineteen agreed accounting adjustments. (R. at 3908-09).

[3] As testified by DEC witness Kim Smith,

> Q So y'all were not aware that ORS was contesting these charges? Is that what you're saying?
>
> A At what point?
>
> Q Well, at any point.
>
> A Well, we knew they were when they filed their rebuttal – or their surrebuttal, I guess, which was Tuesday evening at five o'clock, and we came into hearing Thursday morning at ten.

The Commission heard this matter on March 21-27, 2019 and issued an order May 21, 2019. Among other things, the Commission found that DEC could not recover the South Carolina portion of system-wide coal ash related costs totaling $469,894,472 because those costs were incurred to comply with North Carolina law (R. at 3939) and that DEC could not recover $575,000 in coal ash litigation expenses based on the Commission's finding that DEC did not meet its burden of proof (R. at 3949-50). The Commission further ruled with respect to certain deferral requests made by DEC as follows:

- Carolinas West Control Center (Adjustment #7). The order requires the amortization of prudently incurred deferred depreciation expense totaling $1.4 million over *thirty years* with no return allowed during the deferral or amortization periods. (R. at 3921-23).

- W.S. Lee Combined Cycle Facility (Adjustment #13). The order requires the amortization of prudently incurred deferred depreciation, operations and maintenance ("O&M"), and property tax expenses totaling $7.1 million over *thirty-nine years* with no return allowed during the deferral or amortization periods. (R. at 3923).

- Environmental Costs (Adjustment #18). The order requires the amortization of prudently incurred deferred depreciation expenses totaling $2.1 million over five years without allowing any return during the deferral or amortization period. (R. at 3910-11, 3927-39).

- Advanced Metering Infrastructure (Adjustment #19). The order requires the amortization of prudently incurred deferred depreciation expense totaling $12 million over *fifteen years* with no return allowed during the deferral or amortization periods. (R. at 3939-40).

- Customer Connect (Adjustment #30). The order requires the amortization of prudently incurred deferred O&M costs totaling $3.2 million associated with the implementation of the Customer Connect information system over a period of three years with no return allowed during the deferral or amortization periods. (R. at 3946-47).

- Grid Improvement Costs (Adjustment #35). The order requires the amortization of prudently incurred deferred depreciation, O&M, and property tax expenses totaling $2.8

(R. at 5019:21-20:3). Under prior practice, ORS would have issued additional data requests for any matter on which it sought additional information. (R. at 5019:11-20).

million over a period of five years with no return allowed during the deferral or amortization periods. (R. at 3946-47).

DEC sought rehearing on numerous grounds, including that the treatment of the coal ash compliance costs violated state and federal law, contained factual errors, and was arbitrary and capricious; that coal ash litigation expenses were wrongfully disallowed; and that the denial of a return on the deferrals violated the general principles applicable to rate setting, were inconsistent with past practice, and were arbitrary and capricious. (R. at 4022-35). By order dated October 18, 2019, the PSC declined to revisit its rulings on any of the issues raised in DEC's petition. (R. at 3958-78).

## II. DEP

On November 8, 2018, DEP also filed an Application (the "DEP Application") with the PSC requesting authority to adjust and increase its electric rates, charges, and tariffs effective June 1, 2019. (R. at 142-71). The DEP Application sought the recovery through customer rates of various costs incurred by DEP and deferrals of other costs. This appeal stems from the Commission's handling of the following requests: (1) DEP's request to recover deferred coal ash compliance costs incurred between July 1, 2016 through September 30, 2018 and estimated costs to be incurred from October 2018 through December 2018 plus deferred depreciation and a return on the deferred balances totaling $50 million on a South Carolina retail basis (*Id.* at ¶¶ 7, 15, 20-21, R. at 311:19-12:8, 700:10-16)[4]; (2) DEP's request to recover $389,995 in litigation costs relating to coal ash (R. at 338:5-10, 670:2-74:2); and (3) DEP's request to recover a return on certain deferred costs at a rate equal to its WACC (R. at 142-71 (¶¶ 15, 17, 19-21, 43-46)).

[4] When the full 2018 numbers became available, the final South Carolina retail allocation request was approximately $45 million (R. at 416:12-17, 1222-30). Between July 2016 and December 2018, DEP spent $526.4 million on coal ash basin closure. (R. at 390:15-17).

DEP and ORS agreed on many issues. (*See* R. at 10-11, 19, 65, 429:12-30:19). The parties were not able to reach an agreement with respect to several items, including coal ash compliance costs, returns on deferrals, and coal ash litigation costs.

The Commission heard this matter on April 11-17, 2019 and issued an order on May 21, 2019. Among other things, the Commission found that DEP could not recover the South Carolina portion of system-wide coal ash related expenses totaling $333,480,308 because those costs were incurred to comply with North Carolina law.[5] (R. at 104-05). The Commission also found that DEP could not recover $390,000 in coal ash litigation expenses based on the Commission's finding that DEP did not meet its burden of proof. (R. at 107). In addition, the Commission ruled with respect to certain deferral requests as follows:

- GridSouth, Fukushima/CyberSecurity (Adjustment #17). The order requires the amortization of prudently incurred deferred O&M expenses totaling $8.975 million over five years without allowing any return during the deferral or amortization periods.

- Environmental Costs (Adjustment #18). The order requires the amortization of prudently incurred deferred depreciation expenses totaling $227,000 over five years without allowing any return during the deferral or amortization period.

- Advanced Metering Infrastructure (Adjustment #19). The order requires the amortization of prudently incurred deferred depreciation expenses totaling $640,000 over a period of *fifteen years* without allowing any return during the deferral or amortization period.

[5] DEP's coal ash compliance costs for 2015 through June 30, 2016 were approved by the PSC on a deferred basis in DEP's 2016 rate case. (*See* R. at 148-49 (¶ 15), 152 (¶ 20), (referencing PSC Order 2016-871 in Docket No. 2016-227-E (2016), which states "[T]he Settling Parties agreed that coal ash expenses incurred from January 1, 2015, through June 30, 2016, will be included and amortized over fifteen (15) years at the approved return in this rate case. . . . The Commission finds and concludes that this provision of the Settlement Agreement is just and reasonable in light of the evidence presented, particularly given the fact that agreement of the inclusion of certain coal ash expenses in this case has no precedential effect and will not prejudice the position of any Party in any future proceeding before the Commission."). As discussed further below, the disallowance figure in this case included these costs previously allowed by the PSC.

- Customer Connect (Adjustment #30). The order requires the amortization of prudently incurred deferred O&M expenses totaling $923,000 over a period of three years with no return allowed during the deferral or amortization periods.

- Grid Improvement Costs (Adjustment #35). The order requires the amortization of prudently incurred deferred depreciation, O&M and property tax expenses totaling $848,000 over a period of five years without allowing any return during the deferral or amortization periods.

(R. at 91-101, 107-08).

DEP sought rehearing on several grounds, including that the treatment of the coal ash expenses violated state and federal law, contained factual errors, and was arbitrary and capricious; that coal ash litigation expenses were wrongfully disallowed; that the treatment of the deferrals violated the general principles applicable to rate setting and were not treated consistent with past practice and were arbitrary and capricious.[6] (R. at 172-87). By order dated October 18, 2019, the PSC declined to revisit its rulings on these issues. (R. at 139-40).

The Companies served notices of appeal from these orders on November 15, 2019.

## FACTS

For decades, the Duke Entities have provided electricity to customers in North Carolina and South Carolina (collectively, the "Carolinas") through a shared system and have allocated the costs of providing that service among those customers. (R. at 292:7-13, 620:12-20, 4056:11-13, 4106:12-13). The PSC has traditionally approved an allocation by DEC of those system costs approximately 76% to North Carolina retail and wholesale and 24% to South Carolina retail, and the PSC has traditionally approved an allocation by DEP of those system costs approximately 90% to North Carolina retail and wholesale and 10% to South Carolina retail. (R. at 1220, 4739:8-11).

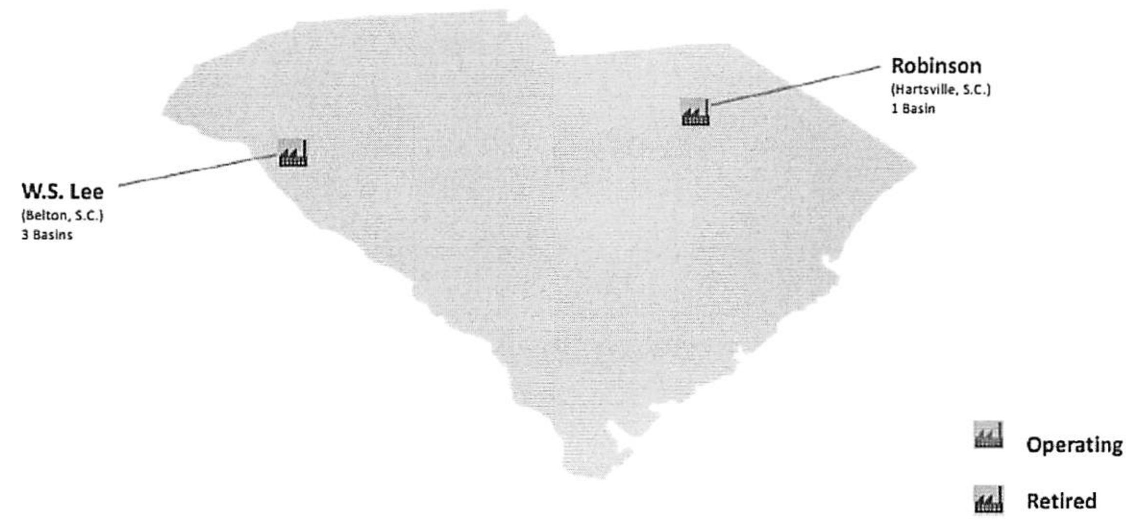
[6] DEP successfully sought rehearing with respect to litigation expenses it incurred defending a claim brought by Certainteed relating to an uneconomic contract to sell gypsum created as a byproduct of the use of scrubbers at DEP's coal-generating plants. (R. at 139-40).

Although there have been some costs through the years that have been directly assigned to one state or the other as state-specific, the majority of costs attributable to the production of electric power, including environmental compliance costs, have been shared between the two states. (*See* R. at 608:17-09:8, 625:22-26:3, 627:10-23, 651:4-13, 4106:6-19, 4603:10-07:8). This cost sharing has included fuel costs and the costs incurred in building and operating generating facilities.

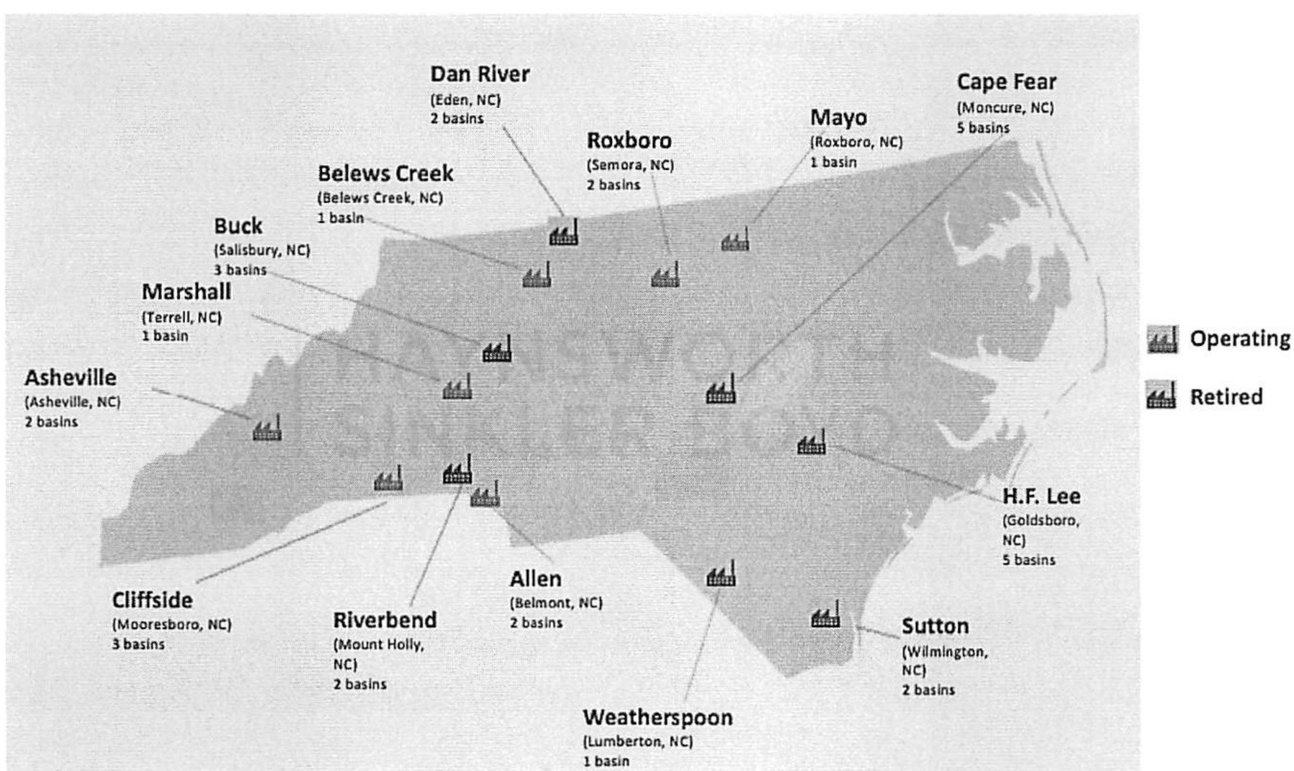
Throughout this period, the Duke Entities minimized their fuel costs to provide efficient and reliable electricity to their customers by using coal-generating plants, most of which are located in North Carolina. (R. at 312:13-13:21, 621:5-17, 1247-48, 5170). The Duke Entities' South Carolina customers enjoyed below-average rates as a result. (R. at 623:1-24:2, 4603:1-8). As agreed by ORS, the Companies' South Carolina customers enjoyed low cost electricity without experiencing the detrimental environmental impacts of having the majority of these plants and their ash basins within their state. (R. at 1007:5-11:7).

The following exhibits provide a helpful summary and history of the Companies' coal-generating plants and ash basin locations in the two states at the time these matters were heard by the Commission:

## Duke Energy South Carolina Sites and Number of Ash Basins




## Duke Energy North Carolina Sites and Number of Ash Basins



**Site Facts - DEC**

| Site | Commercial Operation Date | Generation Capacity (MW) | Retirement Date, if applicable | Possible closure approach | Quantity of ash on site in basins at 7/31/18 (in million tons) | Is a CCR landfill envisioned for the site? |
|---|---|---|---|---|---|---|
| Allen | 1957 | 1127 | n/a | Cap in Place | 16.6MT | No |
| Belews Creek | 1974 | 2220 | n/a | Cap in Place | 12.0MT | No |
| Buck | 1926 | 370 | U3&4 -2011 U5&6 2013 | Beneficiation | 6.5MT | No |
| Cliffside 5 | 1972 | 1396 | n/a | Cap in Place | 7.4MT | No |
| Cliffside 1-4 | 1940 | 210 | 2011 | Onsite landfill | 0 | Yes |
| Dan River | 1949 | 290 | 2012 | Offsite excavation/onsite landfill | 1.1MT | Yes |
| Marshall | 1965 | 2078 | n/a | Cap in Place | 16.8MT | No |
| Riverbend | 1929 | 466 | 2013 | Offsite excavation | .05MT | No |
| WS Lee | 1951 | 200 | 2014 | Onsite landfill | 2.2MT | Yes |

Note: quantities represent basin ash only and do not include fill or landfill ash quantities

**DEC**

**Ash Basin Information**

| Site | Basin | When constructed | Ash in Tons as of 7/31/18 (Millions) | When closed if applicable | CCR Applicable? |
|---|---|---|---|---|---|
| DEC | | | | | |
| Allen | Retired basin | 1957 | 10.4 | 1973 | Y |
| | Active Basin | 1972 | 6.2 | n/a | Y |
| | | | | | |
| Belews Creek | Active basin | 1974 | 12 | n/a | Y |
| | | | | | |
| Buck | Basin #1 | 1956 | 3.6 | 2013 | Y |
| | Basin #2 | 1977 | 2 | 2013 | Y |
| | Basin #3 | 1982 | 0.9 | 2013 | Y |
| | | | | | |
| Cliffside | U1-4 inactive basin | 1957 | 0 | 1977 | Y |
| | U5 inactive basin | 1970 | 2.4 | 1980 | Y |
| | Active basin | 1980 | 5 | n/a | Y |
| | | | | | |
| Dan River | Primary basin | 1956 | 0.7 | 2012 | Y |
| | Secondary basin | 1977 | 0.4 | 2012 | Y |
| | | | | | |
| Marshall | Active basin | 1965 | 16.8 | n/a | Y |
| | | | | | |
| Riverbend | Primary and secondary basins | 1957/1957 | 0.05 | 2014/2014 | N/N |
| | | | | | |
| WS Lee | Primary basin | 1974 | 2.2 | 2014 | Y |
| | Secondary basin | 1978 | 0.03 | 2014 | Y |
| | 1951/1959 inactive basin | 1951 | 0 | 1974 | N |

Site Facts - DEP

| Site | Commercial Operation Date | Generation Capacity (MW) | Retirement Date, if applicable | Possible closure approach | Quantity of ash on site in basins 7/31/18 (million tons) | Is a CCR landfill envisioned for the site? |
|---|---|---|---|---|---|---|
| Asheville | 1964 | 376 | n/a | Offsite excavation | 2.1MT | No |
| Cape Fear | 1923 | 316 | 2012 | Beneficiation | 5.7MT | Yes |
| HF Lee | 1951 | 382 | 2012 | Beneficiation | 6.2MT | No |
| Mayo | 1983 | 727 | n/a | Cap in Place | 6.6MT | No |
| Robinson | 1960 | 177 | 2012 | Onsite landfill | 2.9MT | Yes |
| Roxboro | 1966 | 2439 | n/a | Cap in place | 20.1MT | No |
| Sutton | 1954 | 553 | 2013 | Offsite excavation/onsite landfill | 2.6MT | Yes |
| Weatherspoon | 1949 | 170 | 2011 | Offsite excavation/beneficiation | 2.2MT | No |

DEP

Ash Basin Information

| Site | Basin | When constructed | Ash in Tons as of 7/31/18 (Millions) | When closed if applicable | CCR Applicable? |
|---|---|---|---|---|---|
| | | | | | |
| Asheville | 1964 Basin | 1964 | 2.1 | n/a | Y |
| | 1982 Basin | 1982 | 0 | n/a | Y |
| | | | | | |
| Cape Fear | 1956 Basin | 1956 | 0.4 | 1963 | N |
| | 1963 Basin | 1963 | 0.9 | 1978 | N |
| | 1970 Basin | 1970 | 0.8 | 1978 | N |
| | 1978 Basin | 1978 | 0.8 | 1985 | N |
| | 1985 Basin | 1985 | 2.8 | 2012 | N |
| | | | | | |
| HF Lee | 1950 Basin | 1950 | 0.3 | 1969 | N |
| | 1955 Basin | 1955 | 0.5 | 1969 | N |
| | 1962 Basin | 1962 | 0.9 | 1973 | N |
| | 1982 Basin | 1978 | 4.5 | 2012 | Y |
| | Polishing Pond | 1982 | 0.009 | 2012 | N |
| | | | | | |
| Mayo | Ash basin | 1983 | 6.6 | n/a | Y |
| | | | | | |
| Robinson | Ash Basin | Mid 1970s | 2.9 | 10/1/2012 | Y |
| | | | | | |
| Roxboro | East Ash Basin | 1963 | 7.1 | 1983 | Y |
| | West Ash Basin | 1973 | 13 | n/a | Y |
| | | | | | |
| Sutton | 1971 Basin | 1971 | 1.5 | U1 & U2 11/27/13<br>U3 11/4/13 | Y |
| | 1984 Basin | 1984 | 1.1 | U1 & U2 11/27/13<br>U3 11/4/14 | Y |
| | | | | | |
| Weatherspoon | Ash Basin | 1955 | 2.2 | 9/30/2011 | Y |

(R. at 1247-50, 5170-73 (exhibits resized)).

Coal Combustion Residuals ("CCR" or "coal ash") are an unavoidable byproduct of burning coal to generate electricity in a coal-generating plant. (R. at 706:2-3, 4503:2-3); *see also* Hazardous and Solid Waste Management System; Disposal of Coal Combustion Residuals From Electric Utilities, 80 Fed. Reg. 21,302, 21,303 (April 17, 2015) (codified at 40 C.F.R. pts. 257 & 261) ("CCR Rule"). Here, the coal ash was created in the production of electricity for transmission and distribution in the Carolinas. (R. at 312:13-13:21, 4076:22-77:23). These plants and their coal ash basins must comply with federal environmental laws and the state environmental laws of the state where each plant is located— regardless of whether the electricity generated is consumed in South Carolina or North Carolina.

Over time, the standards for the handling of coal ash have changed due to state and federal regulatory activity. (*See* R. at 708:1-14:15, 1251, 4505:1-24:19, 5174). These standards have evolved from the exclusive use of coal ash basins and impoundments to the gradual introduction of dry ash handling and landfilling as the industry adapted to changing environmental regulations. (*Id.*) Between 2014 and 2015, federal and state regulations fundamentally changed how utilities operate and manage CCR, most dramatically with regard to ash basins. (*See id.*)

The record in each case includes an explanation of the regulatory history with respect to CCR as well as what is currently required in North Carolina, South Carolina, and under the CCR Rule. (*See* R. at 652:20-53:11, 657:15-23, 708:1-14:15, 1251, 1264-1313, 4505:1-24:19, 5175, 5187-266). The CCR Rule was proposed in 2010 as a set of nation-wide criteria addressing the disposal of CCR and the operation and closure of active CCR landfills and existing and inactive CCR surface impoundments. 80 Fed. Reg. 21,302, 21,303. Given the nature of CCR and citing "the risks posed to human health and the environment by certain CCR management units," the Environmental Protection Agency ("EPA") promulgated national standards "to ensure that the

[CCR regulation] . . . effectively address[es] . . . the human health and environmental risks associated with the disposal of CCRs . . . ." *Id.* at 21,411.

The EPA promulgated the CCR Rule pursuant to the authority granted under the Resource Conservation and Recovery Act ("RCRA"). RCRA was adopted to ensure that waste management practices are "conducted in a manner which protects human health and the environment." 42 U.S.C.A. § 6902(a). Within RCRA, Congress stated that it "declares it to be the national policy of the United States . . . to minimize the present and future threat to human health and the environment." 42 U.S.C.A. § 6902(b).

The CCR Rule imposes a set of minimum requirements, and encourages states to adopt plans at least as stringent as the CCR Rule.[7] (R. at 609:9-22). As stated in the preamble,

> In order to ease implementation the regulatory requirements for CCR landfills and CCR surface impoundments, EPA strongly encourages the states to adopt at least the federal minimum criteria into their regulations. EPA recognizes that some states have already adopted requirements that go beyond the minimum federal requirements; for example, some states currently impose financial assurance requirements for CCR units, and require a permit for some or all of these units. This rule will not affect these state requirements. *The federal criteria promulgated today are minimum requirements and do not preclude States' [sic.] from adopting more stringent requirements where they deem to be appropriate.*

[7] The EPA's long-standing policy has been to establish minimum standards, leaving states to adopt more stringent standards. *See* Criteria for Classification of Solid Waste Disposal Facilities and Practices, 44 Fed. Reg. 53,438, 53,439 (September 13, 1979) (codified at 40 C.F.R. pt. 257) (''the standards established in the criteria constitute minimum requirements. These criteria do not preempt other state and federal requirements.''); *see also* Guidelines for Development and Implementation of State Solid Waste Management Plans, 44 Fed. Reg. 45,066, 45,066 (July 31, 1979) (codified at 40 C.F.R. pt. 256) (''EPA establishes only 'minimum' requirements under this portion of the Act which should not prevent States from developing broader programs or stricter standards under authority of State law.").

80 Fed. Reg. 21,302, 21,430 (emphasis added).[8] The EPA further explains that the states play a critical role "in implementation and ensuring compliance with environmental regulations" and that it "expects that states will be active partners in overseeing the regulation of CCR landfills and CCR surface impoundments." *Id.* In addition to acknowledging that states are free to adopt regulatory requirements that are more stringent than the federal baseline standards, the CCR Rule specifically identified the release of CCR into watersheds as falling within the scope of federal and state regulatory authority. *See id.* at 21,364.[9]

South Carolina and North Carolina have taken similar approaches to address coal ash basins, albeit utilizing different regulatory mechanisms. In South Carolina, the Department of Health and Environmental Control ("DHEC") pursued consent agreements and voluntary commitments from electric utilities that have generated CCR. (R. at 1235-46 (H.B. Robinson Plant in Hartsville, South Carolina), 5159-69 (W.S. Lee Plant in Belton, South Carolina). The Duke

---

[8] The CCR Rule has been in a state of flux since 2018. In *Util. Solid Waste Activities Grp. v. EPA*, 901 F.3d 414, 449 (D.C. Cir. 2018) ("USWAG"), the D.C. Circuit sent portions of the CCR Rule back to the EPA for revision, finding, among other things, that "the EPA has statutory authority to regulate inactive impoundments." Since that time, the agency has worked to comply with the USWAG ruling, most recently with proposed revisions in December 2019 and March 2020. Hazardous and Solid Waste Management System: Disposal of Coal Combustion Residuals From Electric Utilities; A Holistic Approach to Closure Part A: Deadline To Initiate Closure, 84 Fed. Reg. 65941-01 (proposed December 2, 2019) (to be codified at 40 C.F.R. pt. 257); Hazardous and Solid Waste Management System: Disposal of CCR; A Holistic Approach to Closure Part B: Alternate Demonstration for Unlined Surface Impoundments; Implementation of Closure, 85 Fed. Reg. 12456-01 (proposed March 3, 2020) (to be codified 40 C.F.R. pt. 257).

[9] The waterways of the Carolinas are in many respects inextricably intertwined. For example, the Pee Dee River basin links the two states with the Great Pee Dee River as the "primary Interstate" for the flow of water between the two states. Melissa Griffin, Understanding River Basin Flooding in the Carolinas, Coastwatch Currents, N.C. State University (Sept. 18, 2018) (accessed at https://ncseagrant.ncsu.edu/currents/2018/09/understanding-river-basin-flooding-in-the-carolinas/). Other river basins such as the Yadkin, Santee, Cape Fear, and Neuse affect both states. *Id.*; *see also* S.C. Code Ann. § 50-1-50 (identifying bodies of water (rivers, lakes, and creeks) that are shared between the two states); *South Carolina v. North Carolina*, 558 U.S. 256 (2010) (recognizing the waters of interstate stream between North Carolina and South Carolina).

Entities entered consent agreements with DHEC, as have other South Carolina electric utilities. (*See id.*, R. at 1163:6-64:7, 4998:21-99:4).

North Carolina implemented a statutory scheme, the Coal Ash Management Act of 2014 ("CAMA"). N.C.G.S. §§ 130A-309.200-.231. Both CAMA and the consent agreements require the closure of all ash basins. (R. at 702:7-8. 4999:9-10). However, the consent agreements require the excavation of all South Carolina ash basins, while CAMA only explicitly requires the excavation of some basins, leaving open the potential for the "cap in place method" in other locations. (R. at 701:19-02:6, 4998:21-99:8). In this respect, South Carolina's approach is more stringent than that of North Carolina. (*See* R. at 657:13-23, 4684:2-6). The Companies' witness Jon Kerin provided a detailed analysis of what was required at each location in each case, together with a listing of the applicable law, regulation, or consent agreement giving rise to that obligation. (R. at 5261-66, 1310-13).

The Duke Entities sought approval and recovery of North Carolina's allocated share of these costs according to the traditional allocation percentages in North Carolina Utilities Commission ("NCUC") Docket Nos. E-2, Sub 1142 and E-7, Sub 1146. The NCUC approved these requests, including the costs incurred in South Carolina to comply with the DHEC consent agreements. (R.at 653:7-11, 2170-460, 4636:5-9, 5592-993). For example, the NCUC allowed DEP to include 90% of the CCR compliance costs incurred at the Robinson plant in Hartsville, South Carolina to be charged to North Carolina customers. (R. at 627:10-23, 2441).

## STANDARD OF REVIEW

As set forth in S.C. Code Ann. § 1-23-380(5), "[t]he court may not substitute its judgment for the judgment of the agency as to the weight of the evidence on questions of fact." On appeal,

> the court may reverse or modify the decision if substantial rights of the appellant have been prejudiced because the administrative findings, inferences, conclusions, or decisions are:
>
> (a) in violation of constitutional or statutory provisions;
> (b) in excess of the statutory authority of the agency;
> (c) made upon unlawful procedure;
> (d) affected by other error of law;
> (e) clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record; or
> (f) arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of discretion.

*Id.* As recently stated by this Court,

> A decision by the commission is arbitrary "if it is without a rational basis, is based ... not upon any course of reasoning and exercise of judgment, is made at pleasure, without adequate determining principles, or is governed by no fixed rules or standards." *Deese v. S.C. State Bd. of Dentistry*, 286 S.C. 182, 184-85, 332 S.E.2d 539, 541 (Ct. App. 1985) (citing *Hatcher v. S.C. Dist. Council of Assemblies of God, Inc.*, 267 S.C. 107, 117, 226 S.E.2d 253, 258 (1976); *Turbeville v. Morris*, 203 S.C. 287, 315, 26 S.E.2d 821, 832 (1943)).

*Daufuskie Island Util. Co., Inc. v. S.C. Office of Regulatory Staff*, 427 S.C. 458, 463–64, 832 S.E.2d 572, 575 (2019).

## SUMMARY OF ARGUMENTS

The Duke Entities have provided electricity across a shared energy power production and electric transmission and distribution system to customers in the Carolinas for generations. Underlying that shared system is a tradition of cost sharing between those customers based on long-established standards for rate making in the two states. In the orders on appeal, the Commission has set that precedent on its head and found that South Carolina customers should not be responsible for their share of hundreds of millions of dollars in admittedly reasonable and prudently incurred system costs.

The largest single disallowance in each of the cases on appeal is comprised of a large percentage of the reasonable and prudent ash basin compliance costs for the North Carolina ash basins. The Commission disallowed these investments based solely on the policy recommendation of ORS and ORS's expert's erroneous determination as to which costs were incurred to comply with North Carolina law. This disallowance further disregarded the fact that the ash was created and managed to provide inexpensive power across the Carolinas for many years. In other words, the costs were and continue to be incurred to operate and ultimately retire long-term used and useful assets of the system. As explained below and as a matter of law, the Companies are entitled to recover the proportional share of these costs from their South Carolina customers.

In addition, the Commission accepted the Companies' requests to defer certain extraordinary expenses. However, the Commission extended those deferral and amortization schedules beyond the time periods requested by the Companies and refused to provide the Companies a return on much of the unamortized balance over that extended period. Each of these costs has been incurred by the Companies and has been paid by the Companies. By disallowing the requested returns, the Commission has essentially required the Companies to make a zero-interest loan to the Companies' customers. Therefore, the Commission's order requires reversal.

Lastly, the Commission disallowed the Companies' requests to recover coal ash litigation expenses because it found that the Companies had not met their burden of proof for establishing the reasonableness and prudence of these costs. This disallowance raises serious questions about the procedure applied in these cases. In ORS's surrebuttal testimony presented *during* the hearings, ORS asserted *for the first time* that the Companies had failed to meet their burden of proof as to these expenses. This testimony followed months of discovery and the prefiling of volumes of written testimony during which ORS never raised that the Companies had somehow failed to prove the legitimacy of these costs. Because ORS raised its objection so late in the proceedings, the Companies were procedurally unable to respond in full. Rather than giving the Companies the opportunity to justify these expenses as required by this Court's precedent, the Commission simply disallowed them.

Given these errors, the Commission's orders should be reversed. These costs (CCR, deferrals, and coal ash litigation costs) are all properly recoverable from the Companies' South Carolina customers, and the rates should be set at a level that affords sufficient compensation to the Companies.

## ARGUMENTS

By statute, "[e]very rate made, demanded or received by any electrical utility . . . shall be just and reasonable." S.C. Code Ann. § 58-27-810. If the rates established by the PSC are too low to "afford sufficient compensation, the State has taken the use of utility property without paying just compensation and so violated the Fifth and Fourteenth Amendments." *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 308 (1989); *see also* U.S. Const. amend. V; S.C. Const. art. I, § 13(A). "[R]ates which are not adequate to yield a reasonable return on the value of the property used by a utility company to furnish its service to the public are unjust, unreasonable, and confiscatory, and that their effectuation would deprive the utility of its property without due process or just compensation." *Potomac Elec. Power Co. v. Pub. Serv. Comm'n*, 380 A.2d 126, 131 (D.C. 1977). Although "regulation does not guarantee that a utility will achieve its projected revenues, it must provide the utility with a reasonable opportunity to earn a rate of return sufficient to maintain the company's financial integrity, to attract necessary capital at a reasonable cost, and to compensate investors fairly for the risks they have assumed, while protecting the relevant public interests." *Id.* at 132.

As stated by the United States Supreme Court nearly a century ago:

> A public utility is entitled to such rates as will permit it to earn a return upon the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties . . . . The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit, and enable it to raise the money necessary for the proper discharge of its public duties.

*Bluefield Water Works & Improvement Co. v. Pub. Serv. Comm'n of W. Va.*, 262 U.S. 679, 692 (1923). This idea was reaffirmed in *Fed. Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944):

> From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock. By that standard the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.

Together, *Hope* and *Bluefield* provide "the basic principles of utility rate regulation" in South Carolina. *Southern Bell Tel. & Tel. Co. v. Pub. Serv. Comm'n of S.C.*, 270 S.C. 590, 595, 244 S.E.2d 278, 281 (1978); *Patton v. S.C. Pub. Serv. Comm'n*, 280 S.C. 288, 291, 312 S.E.2d 257, 259 (1984); *see also* S.C. Code Ann. § 58-4-10(B) (defining "public interest" to require a balance between "the concerns of the using and consuming public" and the "preservation of continued investment in and maintenance of utility facilities so as to provide reliable and high-quality utility services.").

Consistent with these basic principles, the Companies explained as follows in their Applications:

> This rate increase is further necessary to enable DE Carolinas to maintain its current financial position in light of those significant capital expenditures undertaken to

> meet its customers' needs. In addition to modernization of its generating fleet and closing ash basins, the Company is committed to making South Carolina's air and water cleaner by making its grid smarter to further integrate distributed and small source renewables like rooftop solar. The investments described above by the Company to modernize its generation portfolio and electric infrastructure, to comply with certain environmental requirements associated with ash basin closure, to invest in modernizing the Company's CIS systems, among other projects, are not currently reflected in DE Carolinas' rates. As such, the Company's current rates are not providing sufficient revenues for the Company to meet its day-to-day operating expenses and also provide its investors with reasonable returns on their investments of needed capital.

(R. at 3990-91 (¶¶ 22-24), 153-54 (¶¶ 22-24 (similar)).

It is against this backdrop that the Court must review the PSC orders here. The PSC orders, contrary to law, have impermissibly disallowed significant reasonable and prudent costs, and as a result, the Duke Entities will not be able to charge rates that "yield a reasonable return on the value of the property used by a utility company to furnish its service."

## I. The Commission's rulings with respect to what it deemed "CAMA costs" are arbitrary, capricious, clearly erroneous and in violation of state and federal law given the evidence in the record and the underlying history of cost allocation.

The Duke Entities have a constitutionally protected right to recover their reasonable and prudently incurred expenses of providing electric power to the public. The coal ash at issue was and continues to be produced, managed, and stored as the byproduct of electricity generated and utilized across the Carolinas. The Companies did not seek recovery for "fines, penalties, or costs on which [the Companies had] agreed to forego recovery." (R. at 152-53 (¶ 21), 389:20-22, 685:6-16, 3990 (¶ 21), 4147:9-10). Accordingly, the Duke Entities are entitled to recover their reasonable and prudent ash basin closure compliance costs incurred in the applicable period for each case, regardless of whether those costs were incurred to comply with federal law, South Carolina consent agreements, or North Carolina law. The Commission's rulings suffer from errors of law and their ultimate disallowance rests on numerous factual errors.

Under South Carolina law,

> The "rate base" is the amount of investment on which a regulated public utility is entitled to an opportunity to earn a fair and reasonable return. A public utility's "rate base" represents the total investment in, or the fair value of, the used and useful property which it necessarily devotes to rendering the regulated services.

*Southern Bell Tel. & Tel. Co.*, 270 S.C. at 600, 244 S.E.2d at 283. With respect to the costs for which a utility seeks recovery, "[a]lthough the burden of proof of the reasonableness of all costs incurred which enter into a rate increase request rests with the utility, the utility's expenses are presumed to be reasonable and incurred in good faith." *Hamm v. S.C. Pub. Serv. Comm'n*, 309 S.C. 282, 286–87, 422 S.E.2d 110, 112–13 (1992). "This presumption does not shift the burden of persuasion but shifts the burden of production on to [ORS] or other contesting party to demonstrate a tenable basis for raising the specter of imprudence." *Id.*

No party has argued that the Companies' expenses to comply with CAMA were unreasonable or incurred in bad faith, nor have they claimed those expenses were not prudently incurred. (R. at 964:3-21, 4818:22-19:7, 5077:2-14). It is undisputed that South Carolina customers benefited and continue to benefit from the electricity generated at the North Carolina plants that are the source of the purported CAMA costs. (*See* R. at 1007:5-11:7 (testimony by ORS witness Michael Seaman-Huynh as to the history of cost sharing and benefits to South Carolina of that practice), 810:19-12:25). It is further undisputed that the coal ash located in the Duke Entities' ash basins was produced as a result of providing electricity to customers in South Carolina and North Carolina. The coal ash standards in both states are consistent with the EPA's direction in the CCR Rule. Both states have supplemented the CCR Rule by statute (North Carolina) or consent agreements (South Carolina) tailored to protect the waterways and the health of the populations of each state. For these reasons, and as a matter of law, the costs related to the

CCR basin closures should likewise be borne by customers in both states under the traditional cost allocation methodology.

### A. The Commission impermissibly disallowed the Duke Entities' reasonably and prudently incurred costs by isolating and disallowing what it deemed to be CAMA specific costs.

ORS has not taken the position that cost sharing between the jurisdictions is inappropriate. (R. at 1010:22-11:7, 5108:4-7). Nor can it. Generations of precedent support cost sharing, including approvals of the cost to purchase and burn the coal that necessitated the creation of the Companies' ash basins, together with the cost of constructing the ash basins.

Instead, ORS took the following position:

> ORS recommends that the Commission disallow recovery of coal ash management and disposal expenses related to North Carolina laws and regulations above and beyond federal regulations. It is ORS's position that South Carolina customers be held harmless for the incremental cost differences attributed to North Carolina state laws.

(R. at 5077:2-14, *see* R. at 831:24-32:9, 865:3-9, 913:18-20). In other words, ORS sought to disallow all prudently incurred costs it attributed to CAMA. The Commission rubber-stamped this approach without any discussion of the reasonableness of the expenditures. (R. at 39-52, 3910-11, 3927-39 (accepting in full the ORS position and ORS's witness's calculations as to CAMA attributable costs)).

To further this policy position, ORS retained a witness, Dan Wittliff, to assign a value to costs attributable to CAMA over and above the requirements of the CCR Rule. (R. at 913:14-14:6, 4808:17-22, 4809:13-20). Wittliff candidly testified, "[d]etermining with great precision the CCR cost increases above and beyond what the federal CCR rules require based on the limited information I received during 12 rounds of discovery— I mean it was a lot of information; it just missed the mark in some cases— is a bit like performing brain surgery with a pick ax." (R. at 4751:17-24).

Neither ORS nor Wittliff compared what was required under CAMA with the requirements of the DHEC consent agreements or whether CAMA imposed any obligations in addition to those contained in the DHEC consent agreements. As established in the record, the requirements in each state were similar, and the South Carolina consent agreements were, in some cases, more restrictive than CAMA. (*See* R. at 4683:23-84:6). ORS argued that even though the costs of closing the coal ash basins in South Carolina pursuant to the consent agreements will be paid in large part by North Carolina ratepayers, South Carolina ratepayers should pay no costs attributable to North Carolina's environmental laws. It took this position even though the Companies must comply with these requirements in order to continue to operate for the benefit of customers in both states. ORS did not respond to the rebuttal testimony presented by the Companies that supported allocation of these costs consistent with past history. (R. at 667:2-69:20, 4647:1-49:20).

Wittliff did not offer any opinions about whether ORS was correct in its determination that CAMA related costs should be excluded. (*See* R. at 4809:13-20). Nor did he opine on whether the CCR costs claimed by the Duke Entities were unreasonable or imprudent. (*See* R. at 4818:22-19:5). As he testified in the DEP case,

> Q: Mr. Wittliff, you agree with me, do you not that you have not alleged anywhere in your testimony or exhibits that [DEP] acted imprudently or unreasonably in complying with the federal [CCR] rule, correct?
>
> A: Yes.

(R. at 964:3-21). ORS further admitted that CAMA directly benefitted South Carolinians. (R. at 1007:5-10:6). In addition, on cross-examination, ORS witness Seaman-Huynh agreed that it was prudent for the Companies to comply with CAMA (R. at 998:2-16) and that no one disputed that the costs the Duke Entities incurred in complying with CAMA were reasonable (R. at 998:17-23; *see* R. at 964:3-21).

The Commission accepted ORS's unfounded policy argument and ruled that cost sharing should not occur to the extent the Duke Entities' costs are attributable to CAMA. This rejection of cost sharing was limited to the North Carolina compliance costs— ORS did not suggest the South Carolina customers alone should pay for the closure costs of the South Carolina ash basins as required by the consent agreements. Not only is this position inconsistent with Chapter 58 of the South Carolina Code, it is poor public policy because it encourages the state with sufficient capacity to provide electricity to its own residents (as is the case with North Carolina) to find other ways to increase the costs (through taxation or otherwise) of electricity being supplied to customers in other states who are not perceived as paying their fair share.

The Commission's novel, unfair, and unprecedented policy perspective is not the legal standard for a utility's recovery of its costs. According to this Court, the rates established by the Commission must provide the utility with the opportunity of recovering its reasonable operating expenses, as well as provide a fair and reasonable return on the investments made by the company in providing utility service to its customers. *Southern Bell Tel. & Tel. Co.*, 270 S.C. at 600, 244 S.E.2d at 283. That would include costs incurred incident to providing electricity to South Carolina customers, including compliance costs for the North Carolina ash basins. Disallowance of these costs will directly impact the Companies' "ability to provide safe, clean, reliable electricity" to their customers and could result in additional costs being allocated to South Carolina customers in the future. (R. at 339:31-40:14; *see* R. at 153-54 (¶¶ 22-24), 3990-91 (¶¶ 22-24)).

"Rates which are not sufficient to yield a reasonable return on the value of the property used at the time it is being used to render the service are unjust, unreasonable and confiscatory, and their enforcement deprives the public utility company of its property in violation of the Fourteenth Amendment." *Bluefield*, 262 U.S. at 690. Ultimately, utilities must be permitted to earn "a fair return upon the reasonable value of the property at the time it is being used for the public." *Id.* Under the reasoning in *Bluefield*, the Commission's decisions disallowing these costs amounts to an unconstitutional taking without just compensation under the United States Constitution and South Carolina Constitution. *See* U.S. Const. amend. V; U.S. Const. amend. XIV; S.C. Const. art. I, § 13.

As explained by the Companies' witness, Dr. Julius Wright, even though some costs to serve electric customers may be incurred due to a jurisdiction-specific law, such as differences in property taxes, this does not mean that those costs are not recoverable from all customers who benefit from the electric service activity. (R. at 626:12-26:7, 4606:2-15) It is undisputed that coal ash compliance costs were incurred as a result of producing electricity for the Companies' customers in both South Carolina and North Carolina. The generating units that burned the coal and produced the ash that is subject to the CCR Rule, the DHEC consent agreements, and CAMA provided electricity to customers of the Duke Entities in South Carolina and North Carolina for decades. The costs of building and operating those plants have been shared by the customers of both states on a fair and equitable basis since the plants were brought on line. (*See* R. at 1249-50, 5172-73). Denying the Companies the opportunity to recover these costs would therefore be confiscatory and would unconstitutionally deprive them of property without due process or just compensation. The Commission's disallowance of the recovery of the reasonable and prudent costs the Duke Entities incurred in providing service to their customers based on ORS's flawed and unsupportable policy proposal violates the Duke Entities' constitutional right to recover their reasonable and prudent costs and earn a fair rate of return. *See generally*, *Southern Bell Tel. & Tel. Co.*, 270 S.C. at 595-97, 244 S.E.2d at 280-81; *Potomac Elec. Power Co.*, 380 A.2d at 132-33.

Further, the Duke Entities do not have the option of ignoring South Carolina or North Carolina state law. If the Companies are to continue to supply electric service, they must comply with the environmental laws of both states. It would, therefore, be unreasonable and unlawful to disallow costs the Companies have incurred in following the law of either state— both of which are part of a national framework to protect human health and the environment— to the extent those costs were incurred incident to providing electric power to customers in both states. The inequity of the Commission's decisions is amplified by the fact that North Carolina customers are paying the vast majority of these costs for the South Carolina ash basins.

In disallowing the costs related to the Duke Entities' compliance with CAMA, the Commission relied on the testimony of ORS witness Michael Seaman-Huynh. (R. at 843:7-44:5, 5085:17-86:15). Seaman-Huynh argued that the CAMA related costs should be directly assigned to North Carolina customers and gave as his only support for that argument that the Duke Entities voluntarily directly assigned costs associated with compliance with the South Carolina Distributed Energy Resources Act (S.C. Code Ann. §§ 58-39-100 to -150, "SC DER Act") and the North Carolina Renewable Energy and Energy Portfolio Standards Act (2007 N.C. Sess. Laws 397, "NC REPS Act").[10] (R. at 5085:21-86:1). In his testimony in the DEP case, Seaman-Huynh added additional legislative provisions to his list of direct assignment precedents. (R. at 866:1-5). The Commission cited this testimony in support of its disallowance of CAMA-related costs. (R. at 44, 3938).

The legislative provisions cited by ORS and relied upon by the Commission are readily distinguishable from the remedial provisions of CAMA and reinforce the Companies' argument

[10] Direct assignment is the practice of assigning certain costs to one jurisdiction or another rather than allocating those costs as set forth above.

that the Commission committed legal error in disallowing recovery of CAMA costs. All of these statutory provisions reflect policy decisions by lawmakers that imposed additional, incremental costs on regulated utilities. In every case, the legislative bodies included provisions allowing for the recovery of the incremental costs directly from the customers in their respective states on a prospective basis. CAMA includes no such provision. The legislative provisions cited by ORS are summarized as follows:

- **North Carolina Clean Smokestacks Act** (N.C.G.S. § 62-133.6, "Clean Smokestacks Act"). The Clean Smokestacks Act adopted provisions to require electric utilities to meet higher air quality standards for emissions from coal generation plants. It applied prospectively to plants located in North Carolina and included provisions to permit the utilities to recover their costs of modifying existing plants to meet the new standards directly from North Carolina customers.

- **SC DER Act.** The SC DER Act adopted a number of provisions to encourage the development of alternative energy resources. It applied prospectively only and provided cost recovery for the additional costs imposed on electric utilities directly from South Carolina customers. *See* S.C. Code Ann. §§ 58-39-120 & -130.

- **NC REPS Act.** The NC REPS Act adopted several provisions requiring and encouraging the development of renewable energy resources and the reduction of emissions. It applied prospectively and provided a mechanism for utilities to recover their incremental costs of complying with the Act from North Carolina customers. *See* N.C.G.S. §§ 62-133.8 & -133.9.

- **North Carolina Distributed Resources Access Act** (2017 N.C. Sess. Laws 192, "Distributed Resources Access Act"). The Distributed Resources Access Act provided, on a prospective basis, for the competitive procurement of renewable generation resources in North Carolina and made a number of additional changes in energy policy matters. The legislation imposed additional incremental costs on regulated electricity utilities, but it provided cost recovery mechanisms to allow the utilities to recover those costs from North Carolina customers. *See* N.C.G.S. § 62-113.2 (allowing annual fuel factor recovery of purchases from qualifying facilities and allowing fuel factor recovery of Green Source Advantage administrative costs); N.C.G.S. § 62-110.8(g) & (h) (providing a new rider for the recovery of competitive procurement costs and allowing recovery of solar rebate costs).

The contrast with CAMA is stark. CAMA addressed the environmental impact of coal burning plants that had been operating as system assets for many years. Those plants generated electricity for customers in North Carolina and South Carolina and were paid for by those customers on a system allocation basis. CAMA did not provide for the direct assignment of costs to North Carolina customers because the remediation costs should be recovered on a system basis, just like the other costs of operating these plants.

"A decision is arbitrary if it is without a rational basis, is based alone on one's will and not upon any course of reasoning and exercise of judgment, is made at pleasure, without adequate determining principles, or is governed by no fixed rules or standards." *Deese v. S.C. State Bd. of Dentistry,* 286 S.C. 182, 184–85, 332 S.E.2d 539, 541 (Ct. App. 1985). Where, as here, the Commission makes no findings of fact or conclusions of law, South Carolina courts have found orders to be arbitrary and capricious. As the South Carolina Supreme Court has held, "a recital of conflicting testimony followed by a general conclusion is patently insufficient to enable a reviewing court to address the issues." *Able Communications, Inc. v. South Carolina Pub. Serv. Comm'n,* 290 S.C. 409, 411, 351 S.E.2d 151, 152 (1986). The Commission's decision as to the coal ash compliance costs is not based on any factual finding that the costs were not reasonably and prudently incurred, but rather a policy decision that South Carolina customers simply should not pay the costs of complying with CAMA that are more prescriptive than the requirements of the CCR Rule. This departure from long-standing practice is not supported by any competent findings of fact or conclusions or any fixed rules or standards. In the absence of any such findings, the Commission's orders on this point lack a rational basis, are solely based on the Commission's own will, and are not governed by any fixed rules or standards.

For all of these reasons, the orders with respect to the CCR compliance costs contain errors of law, are arbitrary and capricious, and should be reversed. The coal ash standards of both states are more prescriptive in some respects than the CCR Rule in place at the time this matter was heard. These standards are intended to protect the citizens of each state and the interconnected water quality of both states from the potential adverse effects of CCR. Compliance with these standards directly benefits the water quality and health of South Carolinians.

Given that there was no showing that the costs were not reasonably incurred or that they were incurred in bad faith, the Companies ask that the Court allow these costs on a deferred basis as set forth in the Companies' respective Applications (as adjusted to reflect the actual costs incurred through the end of 2018). In the alternative, the Companies ask that the Court reverse the Commission on this issue and remand with clear instructions that the requested costs must be reviewed consistent with the history of cost sharing and the *Hamm* presumption of reasonableness, regardless of where those costs were incurred. Moreover, the Companies' request to defer any allowed coal ash compliance costs with a return must be allowed for the reasons discussed below.

**B. The Commission's disallowance of what it deemed to be CAMA specific costs violates the Commerce Clause of the United States Constitution.**

In addition, to the extent the Commission's denial of CCR compliance costs was based on the "sovereignty" of the State of South Carolina (R. at 3936-38), the orders violate the Commerce Clause of the United States Constitution, which prevents states from engaging in economic discrimination and burdening the flow of interstate commerce. U.S. Const. art. I, § 8. The Commerce Clause provides that Congress has the power to regulate commerce among the several states. This Court has recognized that "the Commerce Clause is more than an affirmative grant of power; it has a negative sweep as well. Even in the absence of Congressional regulation, the negative implications of the Commerce Clause, often referred to as Dormant Commerce Clause, prohibit state action that unduly burdens interstate commerce." *Travelscape, LLC v. S. C. Dep't of Revenue*, 391 S.C. 89, 103-04, 705 S.E.2d 28, 36 (2011) (internal citations omitted). These concepts have long been applied to the energy industry. *See Commonwealth of Pennsylvania v. State of W. Virginia*, 262 U.S. 553, 596–97, *aff'd sub nom. Com. of Pennsylvania v. State of W.*

*Virginia*, 263 U.S. 350 (1923) ("Natural gas is a lawful article of commerce, and its transmission from one state to another for sale and consumption in the latter is interstate commerce. A state law, whether of the state where the gas is produced or that where it is to be sold, which by its necessary operation prevents, obstructs or burdens such transmission is a regulation of interstate commerce— a prohibited interference.") (citations omitted).

The analysis for assessing whether a state action violates the Dormant Commerce Clause has been recently reiterated by the Eighth Circuit. *LSP Transmission Holdings, LLC v. Seiben*, 954 F.3d 1018 (8th Cir. 2020). As set forth there,

> First, if the law in question overtly discriminates against interstate commerce, we will strike the law unless the state or locality can demonstrate, under rigorous scrutiny, that it has no other means to advance a legitimate local interest . . . Under the dormant Commerce Clause, a law is discriminatory if it benefits in-state economic interests while also inordinately burdening out-of-state economic interests.
>
> Second, even if a law does not overtly discriminate against interstate commerce, the law will be stricken if the burden it imposes upon interstate commerce is clearly excessive in relation to the putative local benefits. This is the *Pike* balancing test [*Pike v. Bruce Church, Inc.*, 397 U.S. 137, 90 S.Ct. 844, 25 L.Ed.2d 174 (1970)]. Essentially, [t]hose challenging the legislative action have the burden of showing that the statute's burden on interstate commerce exceeds its local benefit.

*Id.* (citations and quotations omitted).

When state action discriminates against interstate commerce, it will be struck down unless the discrimination is demonstrably justified by a valid factor unrelated to economic protectionism. *Colon Health Centers of America, LLC v. Hazel*, 813 F.3d 145, 152 (4th Cir. 2016). "A discriminatory measure is 'virtually *per se* invalid,' and will survive strict scrutiny only if it 'advances a legitimate local purpose that cannot be adequately protected by reasonable nondiscriminatory alternatives.'" *Id.* (quoting *Or. Waste Systems, Inc. v. Dep't of Envtl. Quality of State of Or.*, 511 U.S. 93, 99 (1994)).

Here, the Commission's orders with respect to compliance costs are facially discriminatory and put the Duke Entities at a deliberate disadvantage simply because of the interstate nature of their business. The effect of the Commissions' orders is to impose certain environmental costs on North Carolina ratepayers to make the rate base for South Carolina customers lower, even though these costs were incurred in generating electricity in North Carolina to benefit customers in both states. Essentially, the PSC is requiring the Companies' North Carolina customers to absorb the vast majority of the South Carolina CCR compliance costs while refusing to require South Carolina customers to assume any portion of the North Carolina CCR compliance costs that it deems to be attributable to CAMA. It has taken this position without regard to the fact that South Carolina customers benefitted from inexpensive coal generated electricity for generations. This decision, in turn, will make the interstate sale of electricity in South Carolina less attractive in the future.

By contrast, an electrical utility operating solely within a single state and utilizing only intrastate generation and transmission systems has the opportunity to recover all of its environmental compliance costs through rates. Thus, the Duke Entities' ability to earn a reasonable return is decreased solely because they engage in interstate commerce by furnishing electricity to South Carolina customers from generating facilities in North Carolina.

This discrimination represents undiluted protectionism that is not justified by any other valid factors. In its order in the DEP case, the Commission justified its disallowance of the "CAMA costs" by saying only that "to subject South Carolina DEP customers to North Carolina laws which are neither necessary for the provision of power nor which confer any benefits to South Carolina ratepayers would be inappropriate." (R. at 50). The justification in the DEC case was the same: "The Commission . . . has concluded that [DEC] should not be permitted to recover from South Carolina ratepayers the added expenses attributable only to CAMA." (R. at 3939).

The Commission's decision was thus based entirely on the fact that the "CAMA costs" were imposed by North Carolina law, notwithstanding the fact that they were a necessary cost of the interstate nature of the Duke Entities' business and had been reasonably and prudently incurred. The Commission offered no "valid factor unrelated to economic protectionism," *Colon Heath Centers*, 813 F.3d at 151, to support its position, and none exists. Accordingly, the Commission's orders denying recovery of CAMA costs violate the Dormant Commerce Clause and must be reversed.

**C. The Commission's adoption of ORS's unsupported valuation of CAMA specific costs is erroneous.**

In addition to the Commission's erroneous policy decision regarding the disallowance of CAMA costs, the Commission erred in basing the amount of its disallowance solely on the flawed analysis of ORS witness Wittliff. Wittliff's erroneous factual conclusions relating to costs that he deemed to be in excess of what is required under the CCR Rule require reversal under S.C. Code Ann. § 1-23-380(5). In addition, these underlying factual errors deprive the Companies of substantive due process under the Fourteenth Amendment of the United States Constitution and Article I, Section 3 of the South Carolina Constitution.

Ironically, Wittliff was hired by the Attorney General's Office in the Companies' North Carolina rate cases to perform the same task, and he admittedly failed. There, Wittliff asserted that costs DEC incurred to comply with CAMA in excess of those to comply with EPA CCR Rule requirements should be disallowed. The NCUC found that "Witness Wittliff makes no effort to quantify the disallowance he proposed under this theory." (R. at 5910). The NCUC went further by discrediting Wittliff's theory altogether: "Aside from the unsubstantiated theoretical underpinnings of the Wittliff argument, it is not possible to segregate CAMA 2015-2017 costs from EPA CCR costs." (*Id.*)

The PSC's rulings are the opposite of those of the NCUC on this point. For DEC, the PSC accepted Wittliff's proposed disallowances found in Table 5.2 of his direct testimony. (R. at 3938-39, 4786). In that table, Wittliff took what he deemed to be the total claimed DEC system costs, \$876,206,204, and recommended disallowance of \$469,894,472. (*Id.*) In the DEP case, the Commission simply reprinted and adopted a similar exhibit from Wittliff. (R. at 43). There, Wittliff used ORS numbers (which included expenses outside those requested in the DEP Application), determined the amount of the DEP system request from January 1, 2015 through September 30, 2018 to be \$635,040,092, and recommended disallowance of \$333,480,308 of that amount. (*Id.*).

Wittliff conceded he could not make these determinations with any precision. (R. at 4751:17-24). ("I mean it was a lot of information; it just missed the mark in some cases— is a bit like performing brain surgery with a pick ax.") Despite receiving volumes of contracts, purchase orders, and invoices, Wittliff never attempted to tether his CAMA-cost valuation to specific work undertaken by the Duke Entities, nor did he perform an extensive engineering analysis. (*See* R. at 941:3-18 (admitting he applied "surrogate cost estimates"), 966:18-69:8, 4829:21-30:4). Instead, he derived estimates of CAMA-costs from summaries of general activities and total project costs. The Commission then blindly accepted Wittliff's estimates.

In his analysis of CAMA specific expenses, Wittliff adopted a site-by-site approach. There are factual errors underlying those calculations, which require reversal as set forth below:

- **DEC**

  **Riverbend**: The Commission disallowed \$316,680,585, which accounted for all coal ash compliance costs incurred at this location, based upon Wittliff's incorrect testimony that the CCR Rule and other regulatory requirements do not require any remediation at Riverbend. (R. at 3935-39).

  **Dan River**: The Commission disallowed \$116,669,019 in coal ash remediation costs based on Wittliff's testimony that CAMA's alleged accelerated closure timeline caused the Company to incur additional costs, notwithstanding that Wittliff admitted that his calculations for this disallowance were based on an incorrect closure date. (R. at 4825:20-24).

**Multiple Sites:** The Commission based its disallowances for the alleged accelerated timeline costs for DEC sites on Wittliff's calculation using the "weighted average of engineering and planning as a percentage of total project costs", which Wittliff admitted were imprecise estimates and not actual costs. (R. at 4829:21-30:17).

- **DEP**

**All DEP Sites:** Wittliff's calculated disallowances were based on an incorrect test year. DEP's request for coal ash expenses in this rate case covered July 2016 through December 2018. (R. at 45). Wittliff relied on Kerin's Exhibit 10 submitted when the Application was filed, which included costs dating back to January 1, 2015. This mistake was corrected by DEP when DEP filed its errata testimony in January 2019, which included a Revised Kerin Exhibit 10. (R. at 1310-13 (showing total compliance spend of $434,134,431)). Wittliff did not account for these revised numbers in his direct or surrebuttal testimony and instead based his proposed disallowances on the earlier, incorrect numbers and incorrect time period. (*See* R. at 43 (Wittliff Table 5.4 at column heading "Amount Requested (1/1/15-9/30/18, SCORS DEP 10-08)). The Commission blindly accepted the incorrect numbers. (*Id.*)

In addition, the Commission based its disallowances for the alleged increased costs for these sites on Wittliff's calculation using the "weighted average of engineering and planning as a percentage of total project costs," which Wittliff admitted was imprecise and not reflective of actual costs. (R. at 941:3-18).

**Asheville:** The Commission relied on Wittliff's testimony that North Carolina's CAMA rules resulted in additional expenses being incurred due to an accelerated closure schedule, after Wittliff admitted that the closure timeline at Asheville was not affected by CAMA. (R. at 878:15-79:4, 882:1-6, 906 :9-10 (admitting CAMA compliance date for Asheville extended to 2022)).

In addition, the Commission disallowed $98,220,932 in costs incurred at the Asheville plant based on Wittliff's testimony that the Asheville plant could have been remediated via cap in place under the CCR Rule after Wittliff admitted that he had no support for this claim and that he had not conducted any analysis to rebut testimony to the contrary. (R. at 965:18-69:8).

**Sutton:** The Commission relied on Wittliff's testimony that North Carolina's CAMA rules resulted in additional expenses being incurred due to an accelerated closure schedule after he admitted that the CCR Rule timeline would not have reduced costs at this site. (R. at 939:14-19, 977:4-82:5).

> **Weatherspoon:** The Commission disallowed costs incurred at the Weatherspoon site based on Wittliff's claim that Weatherspoon was being treated as a beneficiation site under CAMA after Wittliff admitted that he had made a mistake regarding this assertion. (R. at 982:10-89:13).
>
> **H.F. Lee and Cape Fear:** The Commission tied its disallowance at H.F. Lee and Cape Fear to CAMA's beneficiation requirements being performed at these sites without regard to undisputed evidence that the beneficiation activities at these sites are saving, not costing, DEP customers millions of dollars. (R. at 973:3-14, 975:13-76:21, 2461-68).
>
> **Cape Fear:** The Commission disallowed $33,631,199 which accounted for all coal ash compliance costs incurred to date at this location based upon Wittliff's incorrect testimony that the CCR Rule and other regulatory requirements do not require any remediation at that site. (R. at 40).

In addition to Wittliff's admissions, the Companies provided detailed testimony with respect to each of these sites and why Wittliff's calculations/ opinions were in error. (R. at 4643:7-46:21, 741:4-53:7). For these reasons, in the event the Court does not fully reverse the Commission's determinations with respect to the disallowance of what the Commission deemed CAMA specific costs, the Commission's calculations with respect the amount of the disallowance were "clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record" and must be reversed and remanded for further consideration by the Commission.

## II. The Duke Entities are entitled to recover their prudently incurred coal ash litigation costs.

The Duke Entities sought approval of their litigation costs incurred to support ongoing coal ash litigation efforts— specifically, (1) insurance recovery litigation the Companies initiated to recoup the costs of coal ash remediation, and (2) the defense of enforcement actions brought by non-governmental advocacy groups. (R. at 612:1-14, 671:11-74:2, 2475-3820, 4621:4-13, 4624:8-23, 4650:2-53:16, 6059-100). The Duke Entities' evidence showed that these costs totaled $575,000 in the DEC action and $389,995 in the DEP action.

A substantial portion of the litigation expenses relate to efforts by the Duke Entities to recover sums paid by seeking coverage for coal ash related issues from their liability insurers. (R. at 672:7-14, 4652:7-12. 4727:25-28:11). It was prudent and reasonable for the Duke Entities to pursue coverage under these policies, and it is appropriate that the expenses related to the litigation be included in rates. Any benefits derived from the insurance litigation will flow to the ratepayers who funded such litigation. (R. at 4736:8-23). As a policy matter, utilities should be encouraged to pursue litigation that will ultimately benefit their ratepayers.

With respect to the second category, the Duke Entities presented testimony and exhibits that showed that the coal ash litigation expenses sought did not relate to any criminal matter or to any matter in which it has been determined that the Duke Entities violated environmental laws. (R. at 611:24-12:14, 4624:8-23). Instead, the testimony and exhibits showed that the coal ash litigation expenses relate to normal and prudent business operations. (R. at 612:1-14, 671:11-74:2, 4621:4-13, 4624:8-23, 4650:2-53:16).

These costs were disallowed in both cases because the Companies allegedly failed to carry their burden of proof. (R. at 75, 106-07, 3949). This treatment was arbitrary and capricious and violates the general practice in matters before the PSC. As previously discussed, utilities receive a presumption that their expenses are reasonable, prudent, and incurred in good faith. *Hamm*, 309 S.C. at 286, 422 S.E.2d at 112. Other parties are therefore required to produce evidence that overcomes this presumption, as well as any evidence the utility has proffered that further substantiates its position. *See Utilities Servs. of S.C., Inc. v. S.C. Office of Regulatory Staff*, 392 S.C. 96, 110, 708 S.E.2d 755, 763 (2011) ("[I]f an investigation initiated by ORS or by the PSC yields evidence that overcomes the presumption of reasonableness, a utility must further substantiate its claimed expenditures."). In addition, "[c]onsistent with its obligation to provide

Utility an opportunity to achieve a reasonable return, the PSC was obligated to accord Utility a meaningful opportunity to rebut the evidence presented in opposition to its proposed rates." *Id.* at 107, 708 S.E.2d at 761.

As a component of this scheme of review— the utility's expenses being given a presumption of reasonableness, other parties being provided an opportunity to produce evidence sufficient to overcome this presumption, and the utility proffering evidence that further substantiates its position— and as a matter of law, ORS and other parties bear the burden of production to "demonstrate a tenable basis for raising the specter of imprudence." *Hamm*, 309 S.C. at 286, 422 S.E.2d at 112 (citing S.C. Code Ann. §§ 37-6-605, 58-3-190, & 58-27-1960). Put another way, a utility's presumption of reasonableness "shifts the burden of production on to the Commission or other contesting party." *Id.* This burden of production is akin to that necessary in a civil action where a party bears the "responsibility to introduce sufficient evidence on a contested issue to have that issue decided by the fact-finder, rather than decided against the party in a preemptory decision such as directed verdict." *Smith v. Barr*, 375 S.C. 157, 161, 650 S.E.2d 486, 489 (Ct. App. 2007) (citing *Pike v. S.C. Dep't of Transp.*, 343 S.C. 224, 231, 540 S.E.2d 87, 91 (2000)). In the absence of an adverse party meeting this burden of production, the utility's presumption of reasonableness stands.

However, as discussed, should the contesting party meet its burden of production, the utility may provide evidence that further substantiates its position. *See Utilities Servs. of S.C., Inc.*, 392 S.C. at 107-09, 708 S.E.2d at 761-62. The utility must be given "an ample opportunity to explain its expenditures and justify them." *Hilton Head Plantation Utilities, Inc. v. Pub. Serv. Comm'n of S.C.*, 312 S.C. 448, 451–52, 441 S.E.2d 321, 323 (1994).

The Duke Entities were not given that opportunity here. Instead, ORS turned this procedure on its head by surprising the Companies with surrebuttal testimony at the hearing, raising this burden of proof issue for the first time.

ORS has robust discovery and investigatory tools at its disposal. *See* S.C. Code Ann. §§ 58-4-50; 58-4-55; 58-27-160;58-27-190; 58-27-1560; 58-27-1570; 58-27-1580; 58-33-230(F), 58-33-277(B). These enumerated discovery and investigative powers and the commensurate obligation to respond are in addition to the liberal discovery provisions set forth in the Commission's rules and in the South Carolina Rules of Civil Procedure. *See* S.C. Code Ann. Regs. 103-833 ("Any material relevant to the subject matter involved in the pending proceeding may be discovered unless the material is privileged or is hearing preparation working papers prepared for the pending proceeding."); S.C. Code Ann. Regs. 103-835 ("The S.C. Rules of Civil Procedure govern all discovery matters not covered in Commission Regulations.").

Despite the availability of these discovery and investigatory tools at ORS's disposal and the general presumption of reasonableness, ORS recommended disallowance on the basis that sufficient support was not provided by the Duke Entities and the Commission accepted those recommendations. (R. at 69-75, 3949-50). As reflected in the record, the Companies responded to the ORS's discovery requests that were made. (R. at 2475-3820, 4952:3-59:12, 6016-58). In response, as explained by Company witness Kim Smith in the DEC action, the Company supplied over four gigabytes of information, equivalent to approximately 121,000 pages of documentation, excluding the Company's pre-filed testimony. (R. at 5054:2-16). Witness Smith further testified that DEC would have provided the information the ORS claims is now needed in order for the Duke Entities to meet their burden of proof if it had been requested. Additionally, she testified that DEC responded fully to the requests that were made. (R. at 5054:12-56:23). There was similar testimony in the DEP case. (R.at 367:15-23).

There is nothing in the record to suggest that the Duke Entities withheld any information, nor did ORS or any other party file any motions to compel, nor were there any other indications of dispute during the discovery process. ORS sought no and produced no evidence to support its position or to overcome the Companies' presumption of reasonableness, and instead chose to claim the Duke Entities failed to meet their burden because they failed to produce information that was never requested. The Duke Entities responded to discovery that asked for "invoices" and very limited data. (*See* R. at 2475-3820, 6016-21, 6053-58). ORS did not request matter descriptions, factual inquiries, case summaries, contracts, or other documents.

Thus, ORS's tactical decision to raise burden of proof as to these expenses at the surrebuttal stage is patently inconsistent with this Court's charge that the utility must be given "an ample opportunity to explain its expenditures and justify them." *Hilton Head Plantation Utilities, Inc.*, 312 S.C. at 451–52, 441 S.E.2d at 323. Therefore, the procedure here was patently flawed, and the Commission's orders with respect to the coal ash litigation costs should be reversed. The Companies were not afforded the presumption of reasonableness and were not given the opportunity to explain and justify these expenditures.

For these reasons, the Commission's decision disallowing recovery of these expenses should be reversed. At the very least, this issue should be reversed and remanded for further consideration. If it is not and if the insurance litigation proves fruitful, then the proceeds of that litigation should be shared by those who paid for the litigation— shareholders, wholesale customers and retail customers in North Carolina— not retail customers in South Carolina.

## III. The Duke Entities are entitled to recover a reasonable rate of return on prudently incurred deferred costs.

Consistent with past practice as further discussed below, the Duke Entities also sought to defer and amortize certain prudently incurred costs and to recover a return on those deferred costs. The Commission approved the underlying expenses and the request that they be deferred, albeit over a longer period than that sought by the Companies in many instances.[11] (R. at 1-117, 3887-957). The issue on appeal is whether the Duke Entities can recover a return on the full amount of those deferrals through the deferral and amortization periods. The appropriate rate of return on these deferred balances is the WACC determined by the Commission in its ROE analysis.

Generally, regulated utilities recognize and recover costs as they are incurred. This rule applies to ordinary operations and maintenance costs ("O&M"). However,

> [t]here is an exception to this rule [] for expenses deemed "extraordinary." An extraordinary expense is one that is unanticipated and non-recurring. Generally, amortizing an extraordinary expense incurred in the past does not result in retroactive rate-making.

*Porter v. S.C. Pub. Serv. Comm'n*, 328 S.C. 222, 231, 493 S.E.2d 92, 97 (1997 (citations omitted)).

---

[11] This timing element is compounded by the PSC's determination as to the Return on Equity ("ROE"), which it set at a significantly lower level than it has in the past. The orders on appeal were issued just months after the Commission issued PSC Order No. 2018-804 in consolidated Docket Nos. 2017-207-E, 2017-305-E and 2017-370-E (2018). In that consolidated proceeding, the Commission was asked to make a determination of the cost of equity for SCE&G. SCE&G presented the testimony of Robert Hevert, the same witness called by the Companies here. In the SCE&G proceeding, the Commission made the following ruling on the ROE issue:

> In short, the Commission finds that there is ample evidence and reason to conclude that the analyses conducted by Mr. Hevert are accurate and reliable estimates of SCE&G's cost of equity. . . Accordingly, the Commission rejects Mr. Baudino's analysis as flawed and incomplete, concludes that the Company's current cost of equity most likely ranges between 10.25% and 11% as determined by Mr. Hevert, and that the most likely point estimate of the costs of equity is 10.75%, assuming the merger is approved.

PSC Order No. 2018-804 at 89-90. In these cases, based on very similar evidence, the Commission imposed a ROE of 9.5%. (R. at 23-29, 3450-56).

With respect why a utility might seek a deferral, DEP witness Laura Bateman explained,

> Deferrals, by definition, recognize that the Company is incurring a cost that is not currently recovered in customer rates. The Company is incurring costs related to these deferrals. Those costs, whether designated as capital or operating expense for accounting purposes, require cash. That cash must be obtained from the Company's debt and equity investors. And those investors require interest, or a return, on the cash they have invested in the Company. These financing costs (the return on the deferred costs) are a real cost that the Company incurs and to disallow recovery of these costs during the deferral period or the amortization period would be to disallow prudently incurred costs.

(R. at 436:11-20, *see* R. at 365:22-66:11 ("If the Commission accepts these proposals, DEP will not be able to fully recover its prudently-incurred costs."). This practice helps smooth regulatory lag, which in turn means that utility companies will not need to file rate cases as frequently. (R. at 525:7-21, 5021:7-24). It also spreads large extraordinary expenses over a longer period to the benefit of customers. As testified by Bateman,

> [C]ustomers have benefitted from delays of and mitigation of rate increases that directly resulted from the deferrals in this case.
>
> And I think it would be helpful to provide a little background on the deferrals that we're talking about in this case. So if you look at the Fukushima and cybersecurity deferral and the Harris COLA deferred costs, these were both were part of a 2013 deferral petition that specifically stated that the deferrals would enable the Company to delay a rate case filing. At the time, the ORS found value to customers in that benefit and the Commission approved the petition.
>
> In the Company's last rate case, the Company was able to mitigate the increase to customers in that case by delaying recovery of and continuing the deferrals for four of the deferred costs in this case. The Fukushima cybersecurity deferral, the Harris COLA balance, the 2014 Storms, and the coal ash deferral were all part of the settlement in that rate case to defer recovery of those costs. And the ORS was a party to that settlement.
>
> Finally, in the last rate case settlement, we agreed to a two-year stay-out and had the expectation that we would be filing again for new rates effective 1/1/2019 when the stay-out expired to start collecting the costs that we had deferred. However, last spring, the Company determined that it could delay its rate case filing if it were able to secure certain deferrals and file petitions for deferral for costs related to

> Customer Connect, AMI deployment, increases in depreciation rates, and the grid improvement plan. The Commission approved those petitions.
>
> *And even just a 5 month delay in [the increase] benefits customers by anywhere from 10 million to 20 million, depending on the increase ultimately approved by this Commission in the case. So to say that customers have not benefited from the deferrals, it's simply just not based on the facts and not true.*

(R. at 457:9-59:4 (emphasis added)).

ORS and the Commission have agreed that deferral treatment is appropriate in these cases. The only issue is whether the Duke Entities are entitled to a return on all of those deferred costs.

ORS persuaded the Commission to allow the Duke Entities to recover a return only on those expenses that it deemed to be "capital-related." Based on ORS's arguments, the Commission refused to allow a return on what it deemed to be other expenses, including depreciation, O&M, and property taxes. (R. at 91-101, 107-08, 3910-11, 3921-23, 3927-40, 3946-48).

The Commission erred as a matter of law when it classified any portion of the costs it authorized to be included in a deferred account as not capital-related. All of these costs are capital-related and, when placed in deferred account, they lose the classification they otherwise would have received as expenses for ratemaking purposes as a matter of law. In the ratemaking formula, test year expenses included in the Companies' regulated books of account on the operating statement are recovered dollar for dollar in the cost of service calculation. Had the costs in question not been deferred so that recovery was postponed into the future, the costs borne by customers in these cases would have been significantly increased. When deferred, however, they became balance sheet (i.e., capital) costs, a regulatory "asset." Cost recovery is fundamentally altered—

these costs are no longer recovered dollar for dollar in the cost of service calculation. Instead, they are amortized over future years.[12]

Only capital-related costs are recovered in this fashion. The Companies and their shareholders finance the unamortized balance until full recovery is achieved. Thus, the Commission's error with respect to the classification of deferred funds leaves the Companies unable to recover a return of all deferred costs associated with the deferral. (R. at 432:18-38:11, 676:1-78:12, 795:3-96:25, 4185:4-91:11). This is especially true because the Commission has spread the amortization period over many years. (*Id.*)

In the regulatory context of rate adjustments related to known and measurable changes, there is no need to consider the time value of money or the carrying costs of debt because the utility's revenue matches its expenses as they are incurred. By definition, however, deferrals present a situation in which there is a time lag between the company incurring and recovering its costs. In recognition of this lag, the Commission has often allowed a return on deferrals during the deferral period, and, assuming a determination that the costs were prudently incurred, a return on the deferred amount during the amortization period set by the Commission. Such a position is consistent with the regulatory policy that the "just and reasonable rate is set by balancing the interest of the ratepayers and the right of the utility to earn a fair return." *S.C. Cable Television Ass'n v. S.C. Pub. Serv. Comm'n*, 313 S.C. 48, 51, 437 S.E.2d 38, 39 (1993).

---

[12] To further illustrate the arbitrary nature of the Commission's classifications of the underlying deferred costs, costs incurred for identical functions are classified as expenses or as capital expenditures depending on the context. To take a simple example: a Greenville company's office manager travels to Columbia to assess whether to purchase replacement equipment. Should the office manager decide against the purchase, the travel expenses are "operating expenses" charged off in the current period against the company's revenues. If the office manager decides to purchase the equipment, however, proper accounting for the travel expenses is to capitalize them as part of the purchase of the long lived assets to be depreciated over their useful lives.

The PSC has a long history of approving and allowing regulated utilities to engage in deferral accounting where such an approach serves the public interest, as illustrated by the following, non-exclusive list of examples:

- PSC Order No. 10,284 in Docket 10,132 (1957). The Commission allowed United Telephone Company of the Carolinas to create deferral accounts to allow the company to take advantage of IRS approved accelerated depreciation rules on the ground that accelerated depreciation would assist the utility in expanding and modernizing its facilities.

- PSC Order No. 17,300 in Docket No, 17,224 (1973). The Commission approved similar deferral accounting treatment for South Carolina Electric & Gas to allow it to take advantage of accelerated depreciation to assist in financing construction of needed facilities.

- PSC Order No. 96-337 in Docket Nos. 85-78-E, 86-188-E and 91-216-E (1996). The Commission approved the use by Duke Power Company of deferral accounting to "alleviate rate shock" and provide "rate stability" and approved an interim rate decrement rider to allow immediate rate relief to customers.

For DEP, the Commission has previously approved a return on deferrals in PSC Order No. 2014-138 in Docket No. 2013-472-E (2014), approving deferral treatment for both capital and O&M expenses and making no distinction between the two. That order also noted that ORS did not oppose the deferral accounting treatment sought by DEP. *Id.* at 6. With respect to DEC, in PSC Order No. 2013-351 in Docket No. 2013-155-E (2013), the Commission approved deferral accounting of costs related to the addition of DEC's Wayne County combined cycle facility, finding that "granting the Petition will avoid the Company having to undergo a sizeable decline in its earnings, and will aid in helping the Company maintain access to capital on reasonable terms." In addition, the Commission approved the establishment by DEC of the deferral accounts at issue in this proceeding in PSC Order No. 2016-489 in Docket No. 2016-240-E (2016) and PSC Order No. 2018-552 in Docket No. 2018-207-E (2018). Those orders allowed DEC to accrue a WACC return on the deferred balance as has been the practice of the Commission in the past.

ORS did not present any authority directly supporting its position on this matter. (R. at 435:5-35:8). Nor did ORS answer the Duke Entities' data request seeking the accounting authority for its deferral position. (*See* R. at 5013:18-14:10).

As this Court has recently stated,

> [I]n scrutinizing evidence during a ratemaking proceeding, the commission should evaluate the evidence in accordance with objective and consistent standards. *See Utils. Servs.*, 392 S.C. at 113, 708 S.E.2d at 764-65 (acknowledging "the PSC's duty to fix 'just and reasonable' rates" includes evaluating evidence within "the context of an objective and measurable framework"); see also § 58-3-225(A) (2015) ("Hearings conducted before the commission must be conducted under dignified and orderly procedures designed to protect the rights of all parties.").

*Daufuskie Island Util. Co., Inc.*, 427 S.C. at 463, 832 S.E.2d at 574–75. The Commission's rulings are not consistent with past practice and are not made based on any objective accounting principle.

The fallacy of the position advanced by ORS and accepted by the Commission is demonstrated by the testimony of ORS witness David Parcell. Parcell was an expert witness called by ORS to testify on the appropriate cost of capital that should be used by the Commission in calculating a revenue requirement and setting rates. Parcell testified at length about the legal underpinnings of his cost of capital analysis, including a discussion of *Hope* and *Bluefield* as well as leading South Carolina cases. (R. at 597:21-600:16, 4479:21-82:24). Not surprisingly, Parcell conceded that the Commission must set rates for the Duke Entities that allow them a fair opportunity to recover their prudently incurred expenses and a reasonable return on their investment. (R. at 599:3-11, 4481:5-11).

In this discussion, Parcell further explained the Discounted Cash Flow ("DCF") model as an approach to determining cost of capital, which he explained in both cases as follows:

> The DCF model is based upon two fundamental principles. First, DCF is based on the postulate that investors value an asset on the basis of the future cash flows (*i.e.* dividends and ultimate sales in the case of common stocks) they expect to receive from owning the asset. The second DCF principle is that investors value a dollar

> received in the future less than a dollar received today (*i.e.*, the time value of money"). Within this context, the current price of a company's stock is equal to the present value equivalent of the expected dividends and the proceeds from eventually selling the stock. The discount rate that equates the future anticipated dividends and future anticipated selling price with the current market price is the cost of common equity.

(R. at 601:21-02:11, 4483:12-20).

Parcell is, of course, correct that there is a time value of money and that investors value a dollar in hand today more than a dollar to be received in the future. That is why the Commission's refusal to allow the Duke Entities to recover any return or carrying cost on their prudently incurred, deferred expenses is unlawful. The due process principles recognized in *Hope* and *Bluefield* require that the rates of a regulated utility be set to allow a reasonable opportunity to recover the utility's costs incurred in providing service. Requiring amortization of those expenses over periods as long as thirty years without any return fails to allow a reasonable opportunity to recover the expenses and, in fact, insures that the utility will not recover its expenses since the utility will be repaid with less valuable future dollars. The Commission's decision to adopt the ORS position allowing no return on all of these deferred expenses was an error of law requiring reversal of that portion of the orders.

The Commission's orders are also internally inconsistent because they include provisions for carrying costs when they benefit customers. The Commission heard testimony that customers earn a return on a number of costs that they "pre-pay the Company." (*See* R. at 4476:12-77:2 (customers receive a return on the costs being held in the end-of-life nuclear reserve), 4277:12-25 (customers are paid interest on deposits), 4938:9-14 (accumulated deferred income taxes ("ADITs") collected from customers are included in rate base as a credit and thus customers are earning a return on that balance), 4939:7-20 (proposing that customers earn a return on the EDIT balance which would not have existed if the Commission had not ordered that deferral.), 558:12-

20 (end-of-life nuclear reserve would serve as a reduction to rate base), 583:6-12 (proposing that customers earn a return on the EDIT balance which would not have existed if the Commission had not ordered that deferral).

As a further example, the Commission's treatment of the effect of the Tax Cuts and Jobs Act ("TCJA") is inconsistent with its treatment of deferred expenses, demonstrating that the Commission's rulings on deferrals are arbitrary and capricious. Income taxes are an operating expense like depreciation, O&M, and property taxes. Deferred income taxes result from the timing difference between when the Companies collect the funds in rates and when they actually pay the taxes. Because the funds are collected from customers before they are paid as taxes, a regulatory liability is created. The regulatory liability is used as an offset to rate base resulting in substantial savings to customers. If the logic of the Commission's rulings were similarly applied to the impact of the TCJA, rates would significantly increase.

Finally, as the Commission has previously found in the demand-side management and energy efficiency ("DSM/EE") context, deferring the recovery of costs results in the incurrence of carrying costs by the utility. *See, e.g.*, PSC Order No. 2009-373 in Docket No. 2008-251-E (2009) at 24 ("Under PEC's proposal, if the Company defers recovery of its DSM/EE costs, it will incur carrying costs."). Because the expense of the carrying costs associated with the utility's deferred cost recovery is a "legitimate part" of its rate proposal, "the company must be allowed its recovery." *Id.* The Commission concluded that "the recovery of carrying costs is not an incentive, but merely a mechanism to provide for the recovery of costs associated with developing, implementing, and managing the DSM/EE programs." *Id.* This is exactly the dynamic that exists in these cases. The Commission permitted the Companies to defer the recovery of incurred expenses that ORS describes as "reasonable," the Company incurred carrying costs because of this deferral, and the recovery of such carrying costs would not be an incentive but would rather be a mechanism to recover prudently incurred costs.

In these cases, the Commission abandoned this history, ignored the internal inconsistencies, and accepted in full ORS's rote recommendation disallowing a return on any "operating costs." As explained earlier, this distinction between capital and operating expenses has no application to deferred costs. All costs that are deferred cause the utility to incur carrying costs on the unamortized balance.

Given the above, the Commission's orders are confiscatory, fail to provide a just and reasonable rate, and fail to apply objective and consistent standards, substantially prejudicing the Duke Entities. As such, the orders as they relate to the treatment of deferrals must be reversed. *See Daufuskie Island Util. Co., Inc.*, 427 S.C. at 463, 832 S.E.2d at 574-75.

Recovery of the carrying costs on the Companies' deferred expenses complies with the regulatory compact, which itself is based in case law and traditional regulatory principles. The regulatory compact, in essence, is the understanding that "[a] rate-regulated entity incurs costs in order to provide reliable service to customers within its approved service territory in a not unduly discriminatory manner *with the expectation that it will have the right to recover those prudently incurred costs, plus earn a fair rate of return on the capital that has been invested in the business to support reliable utility service*." *See Accounting for the Effects of Rate Regulation* at 5, Edison Electric Institute, 2011 (emphasis added); *see also Southern Bell Tel. & Tel. Co.*, 270 S.C. at 595, 244 S.E.2d at 280-81 ("[T]he governing principle for determining rates to be charged by a public utility is the right of the public on one hand to be served at a reasonable charge, and the right of the utility on the other to a fair return on the value of its property used in the service.").

On the other hand, permitting the utility to establish a deferral and then depriving it of the opportunity to earn a reasonable return on the funds devoted to public service as the Commission has done here is confiscatory and constitutes a taking under the U.S. Constitution. *See Bluefield Water Works & Improvement Co.*, 262 U.S. at 690 ("Rates which are not sufficient to yield a reasonable return on the value of the property used at the time it is being used to render the service are unjust, unreasonable and confiscatory, and their enforcement deprives the public utility company of its property in violation of the Fourteenth Amendment."). As articulated by Justice Ness in his dissent in *Southern Bell*:

> From the investor or company point of view it is important that there be enough revenue not only for operating expenses but *also for the capital* costs of the business. These include service on the debt and dividends on the stock."
>
> The rates established by a utility regulatory commission must not only provide the utility with the opportunity of recovering its reasonable operating expenses, but must also provide a fair and reasonable return on the investments made by the company in providing utility service to its customers.

*Southern Bell Tel. & Tel. Co.*, 270 S.C. at 607-08, 244 S.E.2d at 287 (Ness, J., dissenting in part) (quoting *Hope Natural Gas Co.*, 320 U.S. at 604) (emphasis original). For these reasons, the Commission's findings that, on the one hand, the Companies' deferred expenses are reasonable but, on the other hand, the Companies should not be permitted to recover their respective carrying costs contradicts long-standing precedent and is fundamentally unfair. Utilities must be permitted to recover their expenses, as well as "a fair and reasonable return on the investments made by the company in providing utility service to its customers." *Id.* In these cases, fairness and reasonableness require that the Companies should be permitted to earn a reasonable return on the funds the Commission authorized it to devote to public service.

In this proceeding, it is undisputed that the deferred costs were both prudently incurred and used and useful. The Commission's decision to refuse to allow the Duke Entities to recover any return on substantial portions of their deferrals, combined with the adoption of excessively long amortization periods for the deferrals, prevents the Companies from recovering their prudently incurred expenses as required by the state and federal constitutions. The orders as issued require the equivalent of a lengthy, zero interest loan by the Companies to their customers. Those loans stand as a real and tangible cost to the Companies.

For all of these reasons, the Commission's denial of the Companies' recovery of their carrying costs on all deferred amounts should be reversed. The Companies ask that the Court reverse the Commission and order that a WACC rate of return be applied to all of the deferrals at issue for the entirety of the deferral and amortization periods. In the alternative, the Companies ask that this issue be reversed and remanded to the Commission with a clear directive that a rate of return should be awarded for all approved deferred costs that is consistent with the length of the deferral period.

## CONCLUSION

The Commission failed to set just and reasonable rates in these cases. The Duke Entities ask that the Court reverse and/or reverse and remand the Commission's orders as to each of the arguments presented above. With respect to the coal ash compliance costs, there is no dispute that the costs were reasonably and prudently incurred to provide power across the Companies' systems, including to the Companies' South Carolina customers. Therefore, the Companies seek an order reversing the Commission and allowing those costs. At the very least, the issue should be reversed and remanded to the Commission with the instruction that all reasonably and prudently incurred costs are recoverable, regardless of where those costs were incurred. On the deferral issue, the Companies ask that this Court reverse the Commission and order that that a WACC return is appropriate for the deferrals at issue. In the alternative, the Companies ask that the Court reverse the Commission and remand this issue for a determination as to the appropriate return given the length of the deferral periods. Lastly, on the issue of the coal ash litigation costs, the Duke Entities have demonstrated that the record supports an outright reversal of the Commission's determination and an award of those costs. However, if the Court is inclined to remand this issue, the Commission should be instructed to review the requested expenses through the lens of *Hamm* and the discovery exchanged by the parties.

Respectfully submitted,

______________________________


Heather Shirley Smith (SC Bar No. 102103)
Deputy General Counsel
Duke Energy Carolinas, LLC
Duke Energy Progress, LLC
40 West Broad St., Suite 690
Greenville, SC 29601
heather.smith@duke-energy.com

Frank R. Ellerbe, III (SC Bar No. 1866)
Robert E. Stepp (SC Bar No. 5335)
Robinson Gray Stepp & Laffitte, LLC
P.O. Box 11449
Columbia, SC 29211
fellerbe@robinsongray.com
rstepp@robinsongray.com

Sarah P. Spruill (SC Bar No. 68337)
Haynsworth Sinkler Boyd, P.A.
ONE North Main Street, 2nd Floor
Greenville, SC 29601
sspruill@hsblawfirm.com

Thomas S. Mullikin (SC Bar No. 7939)
Mullikin Law Firm
1308 Broad Street
Camden, SC 29020
tommullikin@mullikinlaw.com

Attorneys for Duke Energy Carolinas, LLC and
Duke Energy Progress, LLC


September 18, 2020